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In the

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1976

No. 76-608

RELIANCE INSURANCE COMPANY,
Petitioner,

VERSUS

DEBOER CONSTRUCTION, INC. and
THE INSURANCE CENTER, INC.,
Respondents.

REPLY BRIEF OF PETITIONER IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT

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December, 1976

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As in the petition and for the purpose of clarity, petitioner Reliance Insurance Company will be referred to as "Reliance," respondent DeBoer Construction, Inc. will be referred to as "DeBoer," and respondent The Insurance Center, Inc. will be referred to as "Insurance Center."

REPLY TO OPPOSITION BRIEF OF DeBOER

DeBoer advances several reasons why this Court should not grant certiorari for the purpose of reviewing this case, with or without certifying to the Supreme Court of Oklahoma for answer the pivotal legal questions which

the Court of Appeals determined were ones of first impression in Oklahoma.

First, DeBoer asserts that because the questions were ones of first impression the decision of the Court of Appeals was not in conflict with applicable Oklahoma law. The fallacy of this contention lies in the fact that the decision of the Court of Appeals was based upon "exceptions" to general rules or principles of law which have never been adopted by the Supreme Court of Oklahoma. Had the Court of Appeals followed to the letter the applicable statutes and existing case law its decision would have been favorable to Reliance, not DeBoer. However, the adoption and improper application of exceptions resulted in a decision in favor of DeBoer. The application of exceptions not previously adopted by the Oklahoma courts would certainly appear to be a departure from existing law.

Secondly, DeBoer argues that the questions are not sufficiently important to the Oklahoma or national surety industry because the Court of Appeals, *by footnote* (540 F.2d 491, fn. 2; Appendix A, p. vi, fn. 2), stated that powers of attorney are still:

> ". . . an effective means of bringing limitations on authority to the third person's attention and defeating his right to rely on other evidence of authority. . . ."

Although the Court of Appeals also held (a) that DeBoer was negligent in failing to read the power of attorney[1] and was not excused under the circumstances from doing so;[2]

[1] 540 F.2d 492; Petitioner's Appendix A, p. vii.

[2] 540 F.2d 491; Petitioner's Appendix A, pp. v-vi.

(b) that Reliance "cannot be liable on the contract [bond] made by Winfrey" and "cannot be liable for his fraud";[3] (c) that DeBoer was under "a duty to exercise reasonable care to ascertain the authority of an agent";[4] and (d) that had DeBoer officers "discovered Winfrey's lack of authority, they would have been bound to inquire of his principal,"[5] the effect of the decision is to impose liability upon Reliance because DeBoer was negligent in not reading the power of attorney which clearly reflected that Winfrey was without authority to issue the bond! In short, the Court of Appeals held that because DeBoer was negligent it was no longer under a duty to inquire. This holding has the effect of rendering powers of attorney an ineffective, not effective, means of bringing limitations on authority to the attention of third parties.

Moreover, the Court of Appeals held valid a verbal promise of a payment bond contrary to the clear terms of the Oklahoma Statute of Frauds.[6] Again, an exception never adopted by the Oklahoma courts was employed in reaching the result.

These questions are vitally important to the surety industry and others which employ the use of powers of attorney because if the Court of Appeals decision is permitted to stand a "third person" could effectively relieve himself of the duty to inquire simply by claiming, rightly or wrongly, that he neglected to read the power of attor-

[3] 540 F.2d 491; Petitioner's Appendix A, p. vi.

[4] 540 F.2d 492; Petitioner's Appendix A, p. vii.

[5] 540 F.2d 491; Petitioner's Appendix A, p. vii.

[6] Title 15, Okla. Stat., § 136 (1971), p. 1376, Vol. 1.

ney and was thus blissfully unaware of the authority limitations. Stated differently, the third party need only testify that he knew a power of attorney existed and assumed that it expressed unlimited authority.

Under such circumstances, commercial sureties and others similarly situated would have no effective means of protecting themselves from liability created by unauthorized contracts short of refusing to use powers of attorney in their business dealings.[7] Construction bonds are normally issued with a penal amount equal to the contract price. The fraudulent bond involved in this case was so written—the penal amount was $925,000, far in excess of the limits set forth in the power. The lower court decision has the effect of permitting the third party (DeBoer) to completely ignore this fact and assume that upon subsequent litigation a court will, in substance, reform the penal amount of the bond to conform with whatever "apparent authority" may have existed had the penal amount been within the scope of the power and had the power been read and relied upon to the third party's detriment.[8]

Such a rule would leave sureties helpless. Although the risk of loss attendant to a construction contract bond

[7] The Court of Appeals attempts to limit the application of its decision to the "facts of this case and the context in which it arises," but does not distinguish the different situations to which it refers when stating that the rule of partial validity should not apply "in all cases involving fraudulent contracts by an agent where the only power exceeded is a limitation on the amount." 540 F 2d 494; Petitioner's Appendix A, pp. xi-xii.

[8] As pointed out in the petition, under Oklahoma law "apparent" authority is created by representations of the principal (such as may be set forth in powers) which come to the knowledge of and are relied upon in good faith by the third party. DeBoer did not read or rely upon any representations made by Reliance.

is measured primarily by the amount and type of contract, coupled with the ability and financial integrity of the contractor/principal, under the Court of Appeals decision a *dishonest* or *negligent* attorney in fact could issue a valid bond in the penal amount of $2,000,000 covering a $2,000,000 contract even though his power of attorney limited him to issuing bonds with penal amounts of $100,000 or less. *The point is that the language in the power to the effect that the attorney in fact is limited to issuing bonds with certain penal amounts is rendered meaningless since a court would be at liberty to reduce the actual penal amount by reformation regardless of the size of the contract or the risks attendant thereto.*

Under the doctrine adopted by the Court of Appeals, a surety or other person prior to issuing a power of attorney would be faced with the question: How may I protect myself from either dishonest or negligent[9] use of a power of attorney if I cannot rely upon the third party being bound by the *penal amount* or other limitations described in the power? The only answer under the Court of Appeals decision is that one cannot protect himself from unauthorized liability.

It is respectfully submitted that the issues are of sufficient importance to justify the attention of this Court.

DeBoer next asserts that certiorari should not be granted for the purpose of certifying for answer to the Supreme Court of Oklahoma legal questions which the

[9] If a surety or anyone else believed a person would use a power dishonestly, then obviously one would not be issued. Limitations are to protect against negligent as well as intentional abuse of authority.

Court of Appeals deemed ones of first impression under Oklahoma law.

Neither in the trial court nor at the Court of Appeals level did Reliance believe that the case involved *legal questions* of first impression under Oklahoma law. It was not until the Court of Appeals rejected the five basic theories[10] of liability employed by the trial court in favor of two *alternative theories*[11] that Reliance had any inclination that the case would be decided upon what the Court of Appeals determined to be questions of first impression. By this time Reliance's only procedural remedy was to petition for rehearing,[12] which it did. Until such time as the Court of Appeals disposed of unsupported fact findings[13] and rejected the basic liability theories (conclusions of law) in favor of Reliance, the case simply was not in a position for certifying questions of law. Certainly there was no compelling reason to certify legal questions concerning *alternative theories* which were not implemented by the trial court.[14] Thus, the contention by DeBoer that Reliance

[10]The theories were: apparent authority to issue a $925,000 bond, fraud, negligence, estoppel and waiver and ratification.

[11]The "partial validity" doctrine and the oral payment bond concept.

[12]Rule 40, Rules of Appellate Procedure.

[13]The trial court made 250 findings of fact and 42 conclusions of law virtually verbatim from those proposed by DeBoer. The Court of Appeals disapproved this "complicated" practice. 540 F.2d 490. Petitioner's Appendix A, pp. iii-iv. Of course, the extensive findings and conclusions made it very difficult to get "on target" with the legal issues, and required Reliance to devote much of its limited briefing space to inapplicable theories.

[14]The judgment of the trial court held Reliance liable under the fraudulent bond for the fulll amount of DeBoer's loss up to $925,000, the penal amount of the bond. The alternative theories were not actually used until the Court of Appeals rejected the principal theories.

should be held guilty of laches for not having requested certification sooner seems totally without merit or reason.

Admittedly, Reliance seeks certification as an alternative to this Court reversing on its own the decision of the Court of Appeals. This is the objective of any appeal or petition for writ of certiorari and is the right of every litigant.

Since *Erie R. Co.* v. *Tompkins*, 304 U.S. 64, 58 S.Ct. 817, 82 L.Ed. 1188 (1938), federal courts have been faced with the problem of ascertaining state law when the state judiciary has not spoken definitively on the matter. Often federal courts were forced to venture guesses, such as was done in this case. To avoid the situation federal courts have developed an abstension doctrine under which they refrain from acting while the litigants seek a statement of law from state courts.[15] The Uniform Certification of Questions of Law Act[16] was created as a suitable technique to assist federal courts in ascertaining state law—particularly questions of first impression. One of the first states to provide for certification was Florida,[17] and the device has been used with some frequence.[18] Likewise, the Supreme Court of Oklahoma has used its power and jurisdiction to answer

[15]*Railroad Commission of Texas* v. *Pullman Co.*, 312 U.S. 496, 61 S.Ct. 643, 85 L.Ed. 971 (1941); 1A Moore's Federal Practice, par. 0.203.

[16]Oklahoma adopted the Act as Title 20, Okla. Stat., §§ 1601-1613 (1973); Petitioner's Appendix D, pp. xxii-xxiv.

[17]Fla.Stat.Ann., Sec. 25.031. Formerly Fla. Appellate Rule 4.61 was used.

[18]See, for example, *Sun Insurance* v. *Clay*, 133 F.2d 735 (5 Cir. 1961); *Green* v. *American Tobacco Co.*, 304 F.2d 70 (5 Cir. 1962), certified question answered 154 So.2d 169, conformed to in 325 F.2d 673 (1963), *cert. den.* 377 U.S. 943 (1964), 84 S.Ct. 1197, 12 L.Ed.2d 229; *Hopkins* v. *Lockheed Aircraft Corp.*, 358 F.2d 347 (5 Cir. 1966), and *Life Ins. Co. of Va.* v. *Shifflet*, 370 F.2d 555 (5 Cir. 1967).

certified questions.[19] Very recently the Fifth Circuit certified a question to the Supreme Court of Alabama concerning performance bonds and the Statute of Frauds, having considered the issue of significant importance to writers of surety bonds in Alabama and the obligees thereunder.[20] This Court has on several occasions certified questions to the highest court of Florida.[21] One such certification was made on the court's own motion[22] because there appeared to be no clear controlling precedents in the decisions of the courts of Florida.

Moreover, this Court seemingly urged the use of the certified question procedure by the circuit courts in *Clay* v. *Sun Insurance*, 363 U.S. 207, 212, 80 S.Ct. 1222, 4 L.Ed.2d 1170 (1960).

Now that the Court of Appeals, based upon settled Oklahoma law, has eliminated all of the legal theories except the two which it has determined to be ones of first impression for Oklahoma, certification would appear appropriate for the first time in these proceedings.

This Court should either grant certiorari and decide the questions or certify them for answer to the Oklahoma Supreme Court or, possibly, direct that the Tenth Circuit Court certify the questions.

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[19] *Travis* v. *Del State Bank*, 553 P.2d 486 (Okl. 1976); *Singh* v. *Cities Service Oil Co.*, 554 P.2d 1367 (Okl. 1976).

[20] *Cincinnati Ins. Co.* v. *City of Talladega*, 529 F.2d 718 (5 Cir. 1976).

[21] *Dresner* v. *City of Tallahassee*, 375 U.S. 136, 84 S.Ct. 235, 11 L.Ed.2d 208 (1963); *Aldrich* v. *Aldrich*, 375 U.S. 75, 84 S.Ct. 184 (1963). same case, 84 S.Ct. 305 (1963).

[22] *Aldrich* v. *Aldrich*, fn. 21.

The remaining portions of the opposition brief are devoted to arguments concerning whether or not the Court of Appeals properly interpreted Oklahoma law or accurately predicted what the Supreme Court of Oklahoma might have to say were the questions presented to it for answer. The original petition for writ of certiorari accurately explains the contentions of Reliance and adequately anticipates arguments of DeBoer. Although DeBoer accuses Reliance of misrepresenting some of the facts and law, a careful study of the petition will reveal that no such misrepresentations were either intended or made. The Court of Appeals decision substantially recites the relevant facts and the law upon which its opinion was based.

REPLY TO OPPOSITION BRIEF OF INSURANCE CENTER

Insurance Center, in the apparent "heat of battle," states (pp. 2-3 of its opposition brief) that Reliance has misstated the facts by not informing the Court that no responsible person with Insurance Center authorized issuance of the fraudulent bonds or knew of their existence or received any benefit therefrom. Perhaps counsel merely overlooked the statements on page 7 of the petition to the effect that the culprit, Winfrey, never sought authority to issue the bonds, never reported them to either Reliance or Insurance Center and never collected or paid any premiums to either Reliance or Insurance Center (Winfrey took a "payoff," not premiums, from Bruce, not DeBoer). No misstatements were either made or intended. The facts were that no one except Winfrey and Bruce had *actual* knowl-

edge of the bogus bonds until many months later when the defaults occurred.

The basic error, as stated in the petition, is that the trial court failed to make appropriate findings to sustain the judgment over for indemnity against Insurance Center, although proposed ones were submitted. The Court of Appeals then misconstrued both the evidence and the law in reversing the judgment over, with the anomalous result that officers of a corporate agency are responsible for their abuse of authority, yet the corporate agency employer is not so responsible even though it was the one with the "agency agreement" and the one, pursuant to that agreement, which requested that powers of attorney be issued to its officers so they might conduct agency business on behalf of the carrier! Insurance Center was Reliance's agent regardless of the fact that Winfrey may have been a "special agent" under and pursuant to the power of attorney. Insurance Center, a corporation, acted through its officers. The agency agreement contemplates that powers will be issued to agency officers and other employees. The agency agreement *does not* contemplate that the corporate agency (Insurance Center) will be relieved of its responsibility and liability simply because powers are issued directly to agency employees.

CONCLUSION

This case presents a classic example of a situation which should result in certifying questions of law to the highest court of a state so that it might properly determine unresolved questions of state law. The statutory authority in Oklahoma is new, yet the Oklahoma Supreme Court has not hesitated to answer questions of even less importance.

Prior to the opinion of the Court of Appeals, the case simply was not in a posture for question certification because there were numerous unsupported factual findings and legal conclusions made by the trial court which could have been and were decided based upon settled Oklahoma law. Once the decision was rendered, Reliance's only procedural remedy was to petition for rehearing on the *alternative* theories which the Circuit Court determined to be ones of first impression under Oklahoma law.

It is respectfully submitted that this Court should grant the writ and either (1) certify the first impression questions to the Supreme Court of Oklahoma for answer, (2) remand the case to the Tenth Circuit so that it might certify the questions or (3) hear and decide the legal questions upon their merits.

Respectfully submitted,

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December, 1976

CERTIFICATE OF SERVICE

I hereby certify that the following named parties,

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required by law to be served in this case, were this day mailed three copies of the foregoing Reply Brief of Petitioner in Support of Petition for Writ of Certiorari, postage prepaid.

Dated: December 19, 1976.

John B. Hayes

John B. Hayes